

# ANALYSIS OF ORIGINAL BILL

## Franchise Tax Board

Author: Vasconcellos Analyst: Davi Milam Bill Number: SB 1163  
Related Bills: See Legislative History Telephone: 845-4073 Introduced Date: 02/23/2001  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Information Technology Training Credit

### SUMMARY

This bill would provide a credit for the cost of certain information technology training.

### PURPOSE OF THE BILL

The purpose of this bill appears to be to encourage training in the field of information technology.

### EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would become effective immediately upon enactment and would be operative for taxable years beginning on or after January 1, 2001.

### POSITION

Pending.

### Summary of Suggested Amendments

Amendments are needed to clarify the definitions of "information technology training" and "small business." Also, amendments are needed to clarify how the \$1,500 or \$2,000 limitation is applied. See "Implementation Considerations" below. Department staff is available to assist the author with these or any other amendments.

### ANALYSIS

#### FEDERAL/STATE LAW

Federal law provides special programs designed to encourage employers to hire or train specified individuals, usually the unemployed or those in need of additional training. Federal programs include the federal Vocational Education Act of 1963 and Job Training Partnership Act. California law makes reference to these federal programs in describing individuals qualified to participate in certain state programs.

Existing federal and state laws allow a deduction for business expenses, including training costs.

Board Position:

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Department Director

Date

**G. Alan Hunter for GHG**

**04/19/2001**

Existing federal and state laws allow a deduction for education expenses incurred to maintain or improve skills required in the taxpayer's business or employment. Costs incurred to meet minimum requirements for a trade or profession or to qualify for a new trade or profession are not deductible.

Existing federal and state laws provide various tax credits that are designed to provide tax relief for taxpayers who must incur certain expenses (e.g., child and dependent care credit) or to influence behavior, including business practices and decisions (e.g., research credits). However, state and federal laws do not currently allow a credit for the cost of training that leads to an IT training certificate.

### THIS BILL

This bill would allow a 100% credit for amounts paid or incurred, not to exceed \$1,500, for information technology training for the taxpayer or any employee of the taxpayer. The credit maximum would be increased to \$2,000 for a small business or if the training takes place in an underserved community. Unused credits could be carried forward indefinitely.

"Information technology training" would be defined as any training that leads to an industry-accepted IT Training Certification.

"Small business" would be defined as an employer that has 200 or fewer employees for each working day in each of 20 or more calendar weeks in the current or preceding calendar year.

"Underserved community" would be defined as an area that is any of the following:

- An empowerment zone or enterprise zone.
- A school district where at least 50% of the students are eligible for free or reduced-cost lunches under the National School Lunch Act.
- A Rural Economic Area Partnership Zone.
- An area declared a natural disaster area by the Governor.

The bill also would require the Governor to establish the Information Technology Training Certification Board to develop a list annually of the latest industry certifications that will qualify for this credit. The Board would submit the list to the National Science Foundation by October 1 of each year.

### IMPLEMENTATION CONSIDERATIONS

This bill would raise the following implementation considerations. Department staff is available to assist the author with any necessary amendments.

- It appears that the author intends for the Information Technology Training Certification Board to develop a list of training classes that will qualify for the credit. However, the Board provides a list of "industry certifications," not "training." Further, the language of the bill does not specify that only training on that list will qualify for the credit. Without an approved list of training eligible for the credit, it may be difficult for taxpayers and department staff to determine if any particular training qualifies for the credit.

Further, the definition of "information technology training" could be interpreted to include classes that are not computer related. For example, if the Information Technology Training Certification Board includes degrees from colleges as an industry-accepted IT training certification, then any general education class that qualifies for the degree would qualify for the credit.

- To determine if a taxpayer is a small business, the number of employees must be reviewed for a two-year period. It may be difficult for taxpayers and department staff to determine if a taxpayer is a small business when employment levels for a business fluctuate around 200 people.
- The credit would be operative for taxable years beginning on or after January 1, 2001. However, the Information Technology Training Certification Board, even if immediately established, would publish the first list of industry certifications on October 1, 2001, at the earliest. Taxpayers will not be able to determine if training qualifies for the credit until the first list is published late in 2001, which arguably reduces the incentive value of this credit.

Further, tax forms are normally printed during October and November of each year to be available to taxpayers on January 1. Printing of this form may be delayed, since the report would be published on October 1 of each year.

- It may be difficult for taxpayers and the department to determine if training took place in an "underserved community."
- It is unclear whether the annual \$1,500 or \$2,000 limitation is per training class, per individual, or per taxpayer.

### TECHNICAL CONSIDERATIONS

The bill uses the term "underserved area" in subdivision (b) but defines the term "underserved community" in subdivision (c). The bill should be amended to use one of the terms consistently through out the bill.

### **OTHER STATES' INFORMATION**

*Florida, Massachusetts, and Minnesota* laws do not provide a credit comparable to the credit allowed by this bill.

*Illinois* provides a credit of 1.6% of training expenses paid for certain educational or vocational training for employees. *Michigan* provides a personal income tax credit for 8% of all fees and tuition paid to a qualified institution of higher learning, not to exceed \$375 per student for each tax year. *New York* provides a refundable personal income tax credit for college tuition expenses. The credit amount varies depending on the amount of costs. The maximum credit is 4% of costs.

The laws of these states were reviewed because their tax laws are similar to California's income tax laws.

## **FISCAL IMPACT**

If the implementation considerations addressed in this analysis are resolved, the department's costs are expected to be minor.

## **ECONOMIC IMPACT**

As currently drafted, the revenue impact of this measure is potentially very significant, in the \$1 billion to \$5 billion range.

The revenue impact of this bill will depend on the number of employees who receive information-technology training. Contacts with industry experts indicated that firms in any industry could provide such training. However, firms in certain industries such as industrial machinery, electrical equipment, and business services are more likely to take advantage of these tax credits. Different assumptions were made for the revenue analysis. Under the conservative scenario, it was assumed that 20% of employees in the above-mentioned industries would receive training in any given year. This resulted in a revenue loss of about \$1 billion. However, since potentially any industry could provide such training, actual revenue losses would exceed a billion dollars annually, perhaps as high as \$5 billion.

## **ARGUMENTS/POLICY CONCERNS**

- Although the bill provides a credit for information technology training that ultimately leads to an industry-accepted IT Training Certificate, the credit is not recaptured if the certificate is not obtained.
- Conflicting tax policies come into play whenever a credit is provided for an expense item for which preferential treatment is already allowed in the form of an expense deduction. This new credit would have the effect of providing a double benefit for that expense item. On the other hand, making an adjustment to reduce the deduction in order to eliminate the double benefit creates a state and federal difference, which is contrary to the state's general conformity policy. In the case of a one-time expense deduction, the reduction of that expense would not create an ongoing difference.
- The credit would be allowed for training expenses paid or incurred either inside or outside California. In fact, the maximum credit amount is increased if the training takes place in a federal empowerment zone and there are only a few located in California. Further, this bill does not restrict the credit to training for employees who are employed within California (and are thus themselves subject to California tax on their earnings).
- This bill does not specify a repeal date or limit the number of years for the carryover period. Credits typically are enacted with a repeal date to allow the Legislature to review the effectiveness of a credit. However, even if a repeal date were added, the department would be required to retain the carryover on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover period limitation since experience shows credits are typically used within eight years of being earned.

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